



UNIVERSITI PUTRA MALAYSIA

**A CASE STUDY ON PHARMA SON BHD -
FOCUSING ON THE VITAMIN C BUSINESS**

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By

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(CASE AUTHENTICITY ACKNOWLEDGEMENT)

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A handwritten signature in black ink, appearing to be 'Ponmalar', is written over a horizontal dotted line. A solid diagonal line extends from the bottom of the signature towards the right.

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EXECUTIVE SUMMARY

In the past years, Pharma Sdn Bhd's revenue was depended on the toll manufacturing business as the major revenue contributor and over-the-counter (OTC) brands. However, the toll manufacturing contract expires in end of 1999 and the management decision was to phase out the toll manufacturing business by the end of 1999 and venture into the ethical market. The ethical business was to start earning revenue in late 1998, with investments breaking even in the year 2002. With the loss of income from toll manufacturing business, alternative revenue was needed to sustain the company until the ethical range starts contributing positively in the year 2003.

Pharma Sdn Bhd is now depended on the OTC business sector for revenue, particularly on the brand Freesia which is a 20 year old brand and currently the market leader in chewable Vitamin C for the adult market. The OTC business sector will be the major revenue contributor for the next five years (1999 - 2003).

The Vitamin C market is highly competitive as many players intensely compete in the open market and direct selling market. Furthermore, new entrants can easily enter the Malaysian market as currently there is no tax imposed on imported Vitamin C nor restrictions on the registration of products. Vitamin C is a vulnerable product to substitution and the chewable Vitamin C products are

undifferentiated and standardised allowing consumers to alternate between brands very easily.

Pharma Sdn Bhd, as the market leader of the adult Vitamin C, is faced with a gradual loss of market share. This is reflected by sales performance of Freesia which was well below the budgeted sale in the year 1998. Another note for concern here, is that the sale of the existing product, have deteriorated whilst competitors had shown a growth of 5 % to 10% for their existing brands.

To be able to sustain it's position as the market leader, the company needs to develop a differentiated and sustainable strategy and apply common sense and experience to understand competitors' moves, if not, the company could loose vital market share in an overnight instance.

PART I : CASE TEXT

1.0 QUARTERLY REVIEW PERFORMANCE MEETING

The Managing Director, Mr. Wee Chee Wah called the meeting to order and welcomed all members present. The meeting then proceeded :

“As all of you are aware, the management has made a decision to phase out the toll manufacturing business by the end of 1999 as our toll manufacturing contract with Aztech, Keano Laboratories and Baytron will be ending this year and neither they nor we are interested in renewing the contract. The management has been looking at a more lucrative market, i.e. the ethical market (doctor’s prescription), which is very promising in terms of returns. The research and development department has been developing the products for the ethical market since 1996. The first launch was in the last quarter of last year. According to the management’s plan, the ethical market was expected to start earning revenue late last year (1998) with investments breaking even in the year 2002.

With the loss of income from the toll manufacturing business, revenue is needed to sustain the company until the ethical range starts contributing positively in the year 2003.”, he continued “ We are now dependent on the over-the-counter (OTC) business sector, particularly on the brand Freesia, which is a 20 year old brand and currently the market leader in chewable Vitamin C for the adult market.

The brand Freesia brings in almost 80% of the revenue for the OTC business sector with the rest coming from the other product lines.

But, judging from the Freesia sales performance for the year 1997 and 1998 (see appendix I and II), you will note that the overall sales for the brand Freesia had increased by 55%, excluding the sales of two new products that were launched in 1998 i.e., Freesia Sugar Free and Junior Multivitamins from RM 737,000 in the year 1997 to RM 1,144,000 in the year 1998. However, the results were well below the budgeted sale of RM 2.14 million for the year 1998. Another note for concern here, is that the sale of Freesia (Orange) Vitamin C for adults has only increased marginally (14%) in comparison to the year 1997.

We urgently need to do something about this as the revenue from the sale of Freesia is vital to keep the company going. The following budgeted sales has to be achieved by the brand Freesia (see appendix III), in order to obtain the needed revenue for the company to be able to sustain itself. Mr. Mahendra will be leading the task force set-up to achieve these targets and will be assisted by Dr. Koh and Ms. Teng.

We also have to bear in mind that we are currently faced with a very competitive and volatile Vitamin C market. Mr. Mahendra will elaborate on this”, said Mr. Wee.

"The vitamin C industry can be segmented by usage and value i.e, effervescents, time release and chewables. The chewables Vitamin C is not much differentiated, hence customer's switching cost is low. Therefore, sales volume seem to be determined by promotions, premium and discounts. In the bulk Vitamin market, hospitals purchase by tender and is very much price driven", said Mr. Mahendra Nathan, the Marketing Manager.

He continued, *" The low switching cost is an incentive for new entrants. The recent example in Malaysia is the entry of Hebron and Organon from Australia and not to mention Citrex from a local supplier - Raza".*

"The manufacturing of chewable and coated Vitamin C except Effervescent is relatively easy. Plants that manufacture tablets can also manufacture Vitamin C, thus a lot smaller independent contract manufacturers are available for a competitor to choose from. Many direct selling companies have their own brands contract manufactured and enter the market easily. A firm only needs large manufacturing batches to keep costs low. As such, large volumes are pushed into the market creating price wars and eroding profits", explained Mr. Mahendra.

Mr. Mahendra then said another possible threat were multivitamins. He says, *" today's consumers prefer a complete vitamin supplement rather than to pop*

many pills each morning. Suppliers of multivitamins are the big guys with the necessary ammunition for promotion and branding. If, the Multivitamins prices drop to the level of Vitamin C prices, consumers will have a field day. If this happens it will certainly force us to revamp our entire business strategy”.

Mr. Kee interjected, “The competitive base could also change if there are mergers (already happening in the world pharmaceutical markets), as bigger players have more firepower. Eroding profits in the low end markets could also see the exit of some players, thus the remaining players have a bigger share”.

Mr. Mahendra continued, “Yet, the real threat is the lack of a good line extension for the brand Freesia. To start with, we launched the Freesia Junior Vitamin C in 1997 and judging from the sales performance (refer to appendix I) the sales has been encouraging. Last year, we produced a sugar free version of Vitamin C for adults and chewable Multivitamin for children. The sugar free version caters for the discerning health conscious adults and has received a good response. The launching of the three products has helped to further differentiate our product but it is not sufficient to sustain our position as a market leader in the long term”.

“If, we still wish to sustain our position as the market leader, it is vital that we develop a complete range of product line for Freesia and this has to be done

immediately. Presently, research and development is working on some new product lines and development is underway. It is imperative for Freesia to move into Effervescent and Time release markets with speed”, emphasised Mr. Mahendra.

“It is important that we are able to sustain the company with minimal support from the parent company as it reflects our capabilities. We should not forget that our pride, bonuses, salary and increments depends greatly on us meeting the stated target “,e

To stay on top of competition, unless the company develops a differentiated and sustainable strategy and applies common sense and experience to understand the competitors’ moves, one could lose vital market share in an overnight instance (Porter, 1985). This is the case in the explosion of generic drugs world-wide.

2.0 COMPANY BACKGROUND

Pharma Sdn Bhd was a wholly owned subsidiary of BCB Berhad, a public listed company in the Kuala Lumpur Stock Exchange (KLSE), under the Healthcare division, see Appendix IV.

Pharma Sdn Bhd's principle activities were manufacturing and packaging of pharmaceuticals and over-the-counter (OTC) dosage forms, with over 30 years of experience. It also does contract repacking and marketing and sales of its own brands. Pharma Sdn Bhd has expertise in the preparation of tablets, capsules, liquids and external preparations for the following medication and medical conditions:

- ◆ Vitamin C and Multivitamins / Minerals
- ◆ Cough & Cold and Cough syrups
- ◆ Tonic
- ◆ Antacid / Antiflatulent
- ◆ Analgesic
- ◆ Antinflammatory
- ◆ Antiasthmatic
- ◆ Antilipid
- ◆ Piles
- ◆ Mouthwash
- ◆ Liniment
- ◆ Antiepileptic
- ◆ Laxatives

Its business activities are divided into three sectors, as exhibited in Appendix V. At the moment, its major revenue comes from toll manufacturing for Aztech, Keano Laboratories and Baytron. However, the toll manufacturing business will cease operation by the end of 1999 and will be replaced by the ethical business, which has started earning revenue in late 1998. Under the OTC business sector, Pharma Sdn Bhd owns 3 brands - Freesia (Vitamin C), Boot's (topical analgesic) and Berry's (tonic).

Its mission statement is to provide Malaysians with medical and healthcare products and services of the highest quality. The objectives of Pharma Sdn Bhd are :-

- ◆ to provide customers with products and services that meet their evolving healthcare needs.
- ◆ to achieve the highest standard in research and development through innovative drug delivery and scientific research.
- ◆ to produce and maintain the highest standard of quality in ethical products and services.
- ◆ to maintain its position as market leader in the Vitamin C industry
- ◆ to provide employees with rewarding and challenging careers.

Pharma Sdn Bhd's organisation structure is shown in Appendix VI.

In this paper, the discussion will be confined to the brand Freesia and the Vitamin C industry.

3.0 ORAGANISATION'S CAPABILITIES

3.1 FINANCIAL

Pharma Sdn Bhd had a paid up capital of RM 3.3 million and appendix VII and VIII shows the past three years, 1996, 1997 and 1998, profit and loss accounts and balance sheet.

“Even though, the company continues to grow at a healthy rate and it had recorded a net profit of RM 1.93 million last year, the cause for concern here is that as of the year 2000, we are faced with a the loss of income from toll manufacturing and the fixed income of RM 1.4 million from the manufacturing fees”, said Ms. Linda Tay, the Finance Manager. She continued, “ income is also generated from contract repacking but, there has been a sharp drop in the year 1998 in comparison to the year 1997 and the same trend is expected to continue for the year 1999. However, it has been forecasted that the drop might only be marginal ”.

“ We are now dependent on the OTC business sector for income, to enable the company to sustain itself. Out of the three brands, about 80 % of the revenue earned comes from the brand Freesia. Freesia has a bigger customer base than the other two brands which are service items with a declining market. “

“Even though, the ethical business has started earning income since last year, it is only expected to contribute positively in the year 2003. Till then, Freesia is expected to achieve a 20% annual sales growth for the year 1999 in comparison to the year 1998 (budgeted), 15% for the year 2000, 10% for the year 2001, 2002 and 2003 respectively.

3.2 MARKETING DEPARTMENT

The marketing department was managed by Mr. Mahendra who had two executives and one secretarial support. Sales was carried out by the distributors but, the marketing of Freesia was controlled by Pharma Sdn Bhd.

“ To do a good marketing programme, an adequate advertising and promotion budget is needed”, said Mr. Mahendra. Here, Mr. Mahendra feels the company is reluctant to spend more on advertising and promotion as the management is more inclined in keeping the fixed cost/expenses down. Mr. Mahendra was unhappy with this policy as he believes that *“unless we are prepared to back the*

product with a well planned advertising and promotion campaign, there is always a high possibility of failure. When a new product is launched its success or failure depends greatly on its marketing plan.”

Mr. Mahendra cited that in consumer marketing, the biggest share of voice transforms into a bigger share of market. He wished that the management would try to understand the importance of “above-the-line” advertising and promotion (e.g. television or cinema advertising) and give the marketing department its due recognition and not treat them as a stepchild. Mr. Mahendra also claimed that though, he and his team have excellent ideas, most of these ideas do not get implemented due to the lack of advertising and promotion funds.

“However, the bigger threat, is the lack of a good line extension for the brand Freesia which will enable it to sustain itself into the 21st century. There are at least three competitors who already have a full umbrella range of products and this attracts customers as it tailors to more specific needs” , said Mr. Mahendra.

3.3 RESEARCH AND DEVELOPMENT DEPARTMENT

Research and development department has all the facilities to capitalise on new growth opportunities that would focus on innovative drug delivery systems/dosage form.

According to Dr Koh Lay Hong, from the registration and product testing team, the company has recently developed Sugar Free Vitamin C for adults and Vitamin C with Multivitamins for children under the brand Freesia Junior. He also said that the research and development department is currently working on a Time Release Vitamin C, Bio C, Acid Free Time Release Vitamin C and Antioxidant + C for adults, under the Freesia brand. However, the department will not develop an effervescent form of Vitamin C due to high capital investment required for manufacturing effervescent.

Many have given various ideas for new line extensions for Freesia but Dr. Koh cited that it will take some time before the product is endorsed and launched in the market.

“More importantly the research and development department’s focus i.e. 80%, is in developing innovative drugs for the ethical market and to do so an investment of RM 2 million has to been spent. From the year 1999 to 2001, a further investment of RM 3 to 5 million would be needed”, said Dr. Koh.

3.4 OPERATIONS / PRODUCTION DEPARTMENT

“The production process requires a very high labour input as its production line is only partly automated as the machinery used in the production line is old, since

1963 ”, said Ms. Mary Teng, the Works Manager. The reasons cited by Ms. Teng was that the machinery were in reasonable working condition and only needed regular servicing and 80% of the current labour force has been with the company for almost 20 years. *“The problem is that we have a high labour cost i.e. older workforce coupled with the limitation of the current machinery, it is difficult to increase productivity, hence higher cost of goods ”*, said Ms. Teng.

She continued by saying that the labour union were not receptive towards the management 's ideas for increasing productivity. In spite of having numerous talks with union representatives, it was very difficult to motivate or convince them. Ms. Teng feels that one of the reasons for the union's behaviour could be due to the stagnation in salary in the last two years. She said that management cannot indefinitely go on increasing the salary of workers. Therefore, the high cost of goods was also due to the high cost of labour.

The amount to refurbish the entire production line would easily cost the company anywhere between RM 5 to 6 million. *“We need to carefully evaluate the investment as we feel that the returns should be financially viable. Furthermore, the research and development department also needs the money”*, explained Mr. Wee.

3.5 QUALITY ASSURANCE DEPARTMENT

According to Mr. Solomon Banos, the Quality Assurance Manager, Pharma Sdn Bhd has a strict in-house quality assurance and quality control activities which is in compliance with GMP guidelines. He said that Pharma Sdn Bhd also complied with the yearly audits by the Drug Control Authority of Malaysia, Aztech and Keano Laboratories International.

Mr. Solomon said that the types of quality assurance test carried out were :

- ◆ Chemical analysis and microbial limit test for products and raw materials
- ◆ Stability study for formulation change, packaging change and new products
- ◆ Conduct testing for deionised water
- ◆ Carry out microbial environmental evaluation
- ◆ Carry out other activities like process validation, self-inspections, vendor audits, customer complaint evaluation, preventive maintenance for laboratory equipment and production machinery.

“However, these strict quality assurance procedures have a tendency to increase the cost of manufactured goods. The marketing department is unhappy with this as they feel the quality assurance procedures are very rigid. They have also suggested that we use a less stringent procedure, i.e. do away with some of the optional procedures.” informed Mr. Solomon. Mr. Solomon stressed that the